

Tax Reduction and Social Policy Bill

Part 1 - Tax Rate Reductions

This part discusses the three items which form part of the reduction in income tax rates. The first item concerns the reduction in the statutory tax rates. The second deals with the changes to the low income rebate, and the third deals with the implications of the tax reductions for provisional taxpayers.

These changes to the income tax rates only apply to individual taxpayers (other than on trustee income). There is no change to the company income tax rate or rates applying to non-individuals.

Income tax rates

Schedule 1, Schedule 14 and Schedule 19 Income Tax Act 1994

Introduction

From 1 July 1996 the income tax scale consists of a bottom rate of 21.5c in the dollar for all taxable income up to \$34,200, and a top rate of 33c on each additional dollar of income.

From 1 July 1997 the income tax scale will consist of a bottom rate of 19.5c in the dollar for all taxable income up to \$38,000. The top marginal tax rate continues unchanged. These changes result in composite tax rates applying for the 1996-97 and 1997-98 income years. The PAYE and RWT rates have been changed accordingly.

Background

The Government announced in its publication *Tax Reduction and Social Policy: Programme: Details* that the aims of the tax reduction programme are to:

- help more people get into paid work
- increase the rewards they get from paid work
- improve the lifetime rewards from training and education.

Reducing the lower tax rate and increasing the top marginal tax rate threshold will increase the rewards available to people who undertake overtime or undertake training or education.

New Zealand has a two-step statutory income tax scale. Before 1 July 1996 the bottom tax rate was 24c on each dollar of income up to \$30,875 per annum and 33c on each subsequent dollar. The two-step tax scale will remain but the rates and thresholds at which the rates apply will change.

Composite rates explained

As many of the proposed tax changes apply from 1 July, part-way through an income year, it is necessary to apply a composite tax scale for that income year. A

composite rate is simply a weighted average of the applicable tax scale applying for the first three months of the income year and the tax scale applying for the last nine months of the income year. For example, from 1 July 1996 the income tax scale will be a bottom rate of 21.5c in the dollar for all taxable income up to \$34,200 and a top rate of 33c on each additional dollar of income. The composite rate for taxable income up to \$30,875 will be 22.125c in the complete dollar. This is the average of the 24c rate for the first three months and the 21.5c rate for the last nine months in the income year.

Key features

Changes taking effect on 1 July 1996

From 1 July 1996 the income tax rates are a bottom rate of 21.5c in the dollar for all taxable income up to \$34,200 and a top rate of 33c on each additional dollar of income. Given the 1 July application date, this results in the following composite rate scale for the 1996-97 income year:

Income	Tax rate per dollar
\$1 - \$30,875	22.125c
\$30,876 - \$34,200	24.375c
\$34,201 and over	33c

This composite tax scale has been inserted into Part B of Schedule 1 of the Income Tax Act 1994. These rates were fixed by the Taxation (Annual Rates of Income Tax 1996-97) Act 1996, which received royal assent on 26 July 1996.

The resident withholding tax deduction rate applying to interest has been lowered from 24c to 21.5c of each dollar of interest income. The amendment applies to any interest paid on or after 1 July 1996. It ensures that the resident withholding tax rate is maintained at the lower statutory marginal tax rate during the 1996-97 income year.

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The withholding rate applying to secondary employment and extra emoluments has been amended. The rate is reduced from 28c to 24c from 1 July 1996. This sets the rate at the effective marginal tax rate applying to income from employment for those who earn between \$9,500 and \$34,200 in the 1996-97 income year.

The weekly PAYE tables are also amended with effect from 1 July 1996, to incorporate the changes to all of the following:

- the statutory tax scale
- the New Zealand Superannuitant surcharge exemption
- the withholding rates applying to secondary employment and extra emoluments
- the low income rebate.

Changes taking effect on 1 July 1997

From 1 July 1997 the marginal tax rate on taxable income up to \$38,000 will be 19.5c in the dollar. The top marginal tax rate continues unchanged. This results in the following composite rate scale for the 1997-98 income year:

Income	Tax rate per dollar
\$1 - \$34,200	20c
\$34,201 - \$38,000	22.875c
\$38,001 and over	33c

The composite tax rate scale for the 1996-97 income year has been replaced by this scale for the 1997-98 income year. These rates will be confirmed during the 1997-98 income year by an annual taxing provision.

The resident withholding tax deduction rate applying to interest subject to resident withholding tax will be reduced from 21.5c to 19.5c from 1 July 1997.

The withholding rate applying to secondary employment and extra emoluments will be reduced from 24c to 21c from 1 July 1997. A new weekly PAYE table has been inserted. The PAYE tables have been amended, with effect from 1 July 1997, to incorporate the changes to:

- the statutory tax scale
- the changes in the New Zealand Superannuitant surcharge exemption
- the withholding rates applying to secondary employment and extra emoluments
- the changes in the low income rebate.

Changes taking effect on 1 April 1998

The tax rates applying to individuals for the 1998-99 income year and subsequent years will be:

Income	Tax rate per dollar
\$1 - \$38,000	19.5c
\$38,001 and over	33c

As there is no change in tax rates applying from 1 July 1998, this tax scale is not a composite tax scale; it reflects the actual tax rates applying for the whole year and subsequent years. Again these rates will need to be fixed by an annual taxing provision passed during the 1998-99 income year. No change in withholding rates, such as the resident withholding tax rate applying to interest, is required because the PAYE and other withholding rates as set on 1 July 1997 remain correct.

Low income rebate

Section KC 1 Income Tax Act 1994

Introduction

The low income rebate is being altered to maintain the effective tax rate of 15c in the dollar which applies to income between zero and \$9,500 per annum. The abatement rate is being altered to ensure that abatement ceases at the point the top marginal tax rate starts.

Background

In the 1995-96 income year the low income rebate applied to natural persons who earned less than \$30,875 of income a year. For superannuitants the rebate was 9.0c for every complete dollar of net income earned up to \$9,500. For other natural persons with net income of less than \$9,500 the rebate was 9.0c for every dollar of assessable income other than interest, dividends, royalties, rents, beneficiary income and taxable distributions (distributions from non-qualifying and foreign trusts). The rebate resulted in an effective tax rate on the first \$9,500 of income of 15c in the whole dollar, being the 24c statutory rate applying in that income year less the 9c rebate.

Those natural persons whose income from personal exertion exceeds \$9,500 or superannuitants whose income exceeds \$9,500 receive the maximum rebate of \$855, reduced by 4c for each dollar of assessable income over \$9,500. The rebate was fully abated when assessable income reached \$30,875. It provided a middle effective tax rate for those who qualified for the low income rebate of 28c in the whole dollar, made up of the 24c statutory rate plus the 4c abatement.

The effect of the changes to the rebate are:

- to maintain the effective tax rate of 15c in the dollar which applies to annual incomes between zero and \$9,500. This means that as the statutory tax rate is reduced there is also a consequential reduction in the value of the rebate.
- to set the abatement rate so that the rebate is fully abated when a person's income reaches the top statutory tax rate. For example, for the 1996-97 income year the rebate is fully abated when income reaches \$34,200, being the threshold above which the 33c in the dollar top marginal rate applies.

Key features

The low income rebate has been reduced so that the composite rebate for the 1996-97 income year is, for super-annuitants, 7.125c for every complete dollar of assessable income earned up to \$9,500. For other natural persons with assessable income of less than \$9,500, the rebate is 7.125c for every dollar of assessable income other than interest, dividends, royalties, rents, beneficiary income and taxable distributions (distributions from non-qualifying and foreign trusts). This reduces the composite statutory tax rate for this year of 22.125c in the dollar to 15c in the dollar.

The abatement rate for incomes between \$9,500 and \$30,875 is 2.875c for each complete dollar. Above \$30,875 the abatement rate is 1.875c, with the rebate fully abated when income reaches \$34,200.

Low income rebate	1995-96 composite rates	1996-97 composite rates	1997-98	1998-99
LIR rebate rate per dollar of income	9.0c	7.125c	5.00c	4.50c
LIR abatement rate per dollar of income				
• \$9,500 - \$30,875	4.0c	2.875c	1.75c	1.50c
• \$30,875 - \$34,200	-	1.875c	1.75c	1.50c
• \$34,200 - \$38,000	-	-	1.125c	1.50c

The low income rebate is further reduced by providing that the composite rebate for the 1997-98 income year is 5c for every complete dollar. This reduces the composite statutory tax rate for this year from 20c in the dollar to 15c in the dollar. The abatement rate for incomes between \$9,500 and \$34,200 is 1.75c for each complete dollar. Above \$34,200 the abatement rate is 1.125c, with the rebate fully abated when income reaches \$38,000.

The low income rebate is further reduced for the 1998-99 income year to 4.5c for every complete dollar, with the abatement rate of 1.5c in the complete dollar applying to income between \$9,500 and \$38,000. Unlike the previous two years' low income rebate figures, this is not a composite rebate.

For those who qualify for the low income rebate, the composite tax rates and the effective tax rates per dollar of income for the 1995-96 to 1998-99 income years are:

Income band	1995/96 (Current scale)		1996/97		1997/98		1998/99	
	Tax rates	Tax rates plus LIR	Composite tax rates	Tax rates plus LIR	Composite tax rates	Tax rates plus LIR	Tax rates	Tax rates plus LIR
\$0 - \$9,500	24c	15c	22.125c	15c	20c	15c	19.5c	15c
\$9,500 - \$30,875	24c	28c	22.125c	25c	20c	21.75c	19.5c	21c
\$30,875 - \$34,200	33c	33c	24.375c	26.25c	20c	21.75c	19.5c	21c
\$34,200 - \$38,000	33c	33c	33c	33c	22.875c	24c	19.5c	21c
\$38,000 and up	33c	33c	33c	33c	33c	33c	33c	33c

Provisional tax

Section MB 2 (1) Income Tax Act 1994/Section 144 Tax Administration Act 1994

Introduction

The uplift factors which provisional taxpayers apply to a prior year's residual income tax to determine the amount of provisional tax payable in the current year have been amended. They have been reduced to ensure that provisional taxpayers do not overpay 1996-97 provisional tax as a result of the tax rate reductions.

Background

With the reduction in tax rates, if natural persons used a prior year's tax liability to determine the amount of provisional tax payable this year they would overpay their provisional tax if no adjustment were made to the last year's payment basis. The amendments apply only to taxpayers whose residual income tax is \$2,500 or more, and whose previous year's taxable income was less than \$70,000.

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A similar adjustment will be considered for the 1997-98 income year in a subsequent tax bill. It is not possible to make the adjustments at this time as the appropriate changes in uplift percentage depend on factors such as the changes in the income levels of natural person provisional taxpayers.

Key features

If 1995-96 year's income is known

A natural person with taxable income up to \$70,000 for the 1995-96 income year may pay provisional tax for the current year on the basis of his or her 1995-96 residual income tax. Previously, a taxpayer paying under this option was required to pay on the basis of 1995-96 residual income plus 5%.

If 1995-96 year's income is not known

There is a change for natural persons with taxable income up to \$70,000 for the 1994-95 income year, who have an extension of time for filing their 1995-96

income tax returns, and whose returns have not been filed. They may pay the first two instalments of provisional tax for the current year on the basis of the 1994-95 residual income tax plus 5%. Previously, taxpayers paying under this option had to pay the 1994-95 residual income plus 10%.

If natural persons with taxable income up to \$70,000 for the 1995-96 income year voluntarily estimate their provisional tax liability but nevertheless underestimate their liability, no underestimation penalty will be imposed if they paid more than their 1995-96 year's residual income tax.

Inland Revenue has written to provisional taxpayers informing them of the changes in the provisional tax payment rules.

Application date

The amendments apply to the 1996-97 income year in relation to provisional tax instalments due on or after 7 July 1996.

Part 2 - Family Assistance

This part deals with the changes to the Family Support and the Guaranteed Minimum Family Income tax credits as well as a new tax credit called the Independent Family Tax Credit.

These changes resulted from the Government's wish to commit a significant proportion of the Budget surplus to boost the income and future prospects of low-middle income families with dependent children.

Independent family tax credit

Section KD Income Tax Act 1994

Introduction

A new family assistance measure, the independent family tax credit (IFTC), is introduced to increase the rewards to those low and middle income families who are not reliant on significant state or ACC support.

Background

The Government introduced the IFTC to encourage families back into the workforce as a means of improving lifetime income and opportunity and to contribute to the extra costs of working, including child care.

Key features

On 1 July 1996 the IFTC will be set at \$7.50 per week per child, with the composite IFTC amount for the 1996-97 income year set at \$292.50 a year.

On 1 July 1997 the IFTC will be set at \$15.00 per week per child, with the composite IFTC for the 1997-98 income year set at \$682.50

The IFTC rate for the 1998-99 income year and subsequent years will be set at \$780 per annum per child (\$15 per week).

The IFTC is not available to families if either spouse receives any of the following forms of income:

- an income-tested benefit (for example, domestic purposes benefit, sickness benefit, training benefit, unemployment benefit)
- New Zealand Superannuation
- veteran's pension
- any basic grant or any independent circumstances grant made under section 193 of the Education Act 1964 or sections 303 of the Education Act 1989, such as an income-tested student allowance (paragraph (g) of the definition of "salary and wages")
- any weekly compensation paid by the Accident Compensation Corporation or its agent, under para-

graphs (h) and (I) of the definition of salary or wages in section OB 1, for a period of more than three consecutive months. The three month term applies because a short-term receipt of ACC compensation paid weekly is not considered to be significant state mandated financial support.

People who have received weekly compensation for more than three months before 1 July 1996 are not entitled to receive IFTC. If they have received compensation for less than three months they may receive IFTC until the date they have received compensation for three consecutive months.

A family which receives supplementary income support, such as the accommodation supplement or a special needs grant may still receive IFTC. It is only receipt of the main income-tested social welfare benefits which excludes eligibility.

Payments of ACC independence allowance and other cash grants which are not earnings-related compensation do not make a person ineligible for IFTC.

A family which suspends an income-tested benefit will not be eligible for IFTC during the period the benefit is suspended. If the family moves off the benefit for a short period and wishes to receive IFTC it should cancel its benefit.

Family credit of tax

New section KD 2 introduces a new term - the "family credit". This credit is determined as follows:

$$a + b - c$$

In this formula:

a is the amount of the Family Support credit (before abatement)

b is the amount of the independent family tax credit (before abatement)

c is the amount of the family credit abatement.

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Abatement

The abatement which previously applied to Family Support now applies to the family credit of tax (which means that it applies equally to Family Support and IFTC). The abatement amount is calculated and first applied to any Family Support credit, with the remainder, if any, being applied to the IFTC. This approach ensures that two families on the same income and in identical circumstances, except that one receives the IFTC and the other does not, receive the same amount of Family Support after abatement. The family credit abatement uses the same rates and thresholds that used to apply to Family Support. They are:

- 18c in the complete dollar of specified income exceeding \$20,000 but not exceeding \$27,000
- 30c for every subsequent dollar of specified income. The abatement is based on the recipient's specified

income, or, if he or she has a spouse, their combined specified income.

Information on implementation

So Inland Revenue can verify entitlement to IFTC, at the end of the income year ACC will transfer to Inland Revenue information on people who have received weekly compensation for a continuous period of three months. This transfer of information is an information matching programme and as such will conform to the requirements of the Privacy Act 1993.

Tax practitioners who want to calculate the amount of IFTC a client is entitled to will need information on the period that the client has been receiving weekly compensation from ACC. Tax practitioners may obtain this information from ACC by completing a form letter which requires the client to authorise the release of the information to the agent.

Family Support

Section KD 2, 2A, 5, 6 Income Tax Act 1994

Introduction

Family Support rates have risen by \$2.50 per child per week from 1 July 1996, and will rise by a further \$2.50 per child per week from 1 July 1997.

Background

Currently, about 250,000 families receive Family Support. Those who received their entitlement during the year have automatically received their increased Family Support entitlement after 1 July each year. We have contacted recipients by direct mail to tell them of the changes.

Those who are eligible for Family Support but do not receive payment during the year will receive their entitlement as an income tax refund once they have filed their tax return.

Key features

On 1 July 1996 Family Support increased by \$2.50 per child per week.

The composite rates which will apply for the 1996-97 income year will be:

- \$2,281.50 for the eldest dependent child
- \$1,501.50 for each further child under 13 years of age
- \$1917.50 if the child is 13 years of age or older.

On 1 July 1997 Family Support will increase by a further \$2.50 per child per week.

The composite rates for the 1997-98 income year will be:

- \$2,411.50 for the eldest dependent child
- \$1,631.50 for each further child under 13 years of age
- \$2,047.50 if the child is 13 years of age or older.

For the 1998-99 and subsequent income years the annual Family Support entitlement is:

- \$2,444 for the eldest dependent child
- \$1,664 each for other dependent children, if they are under the age of 13
- \$2,080 for a child of 13 years of age or older.

These are not composite rates but represent the on-going Family Support position.

The sections which deal with joint custody have been changed to clarify that persons can be dependent children when aged 18 if they are not financially independent and are still attending school or a tertiary educational establishment. The changes to joint custody are, in essence, a simplification of the previous provisions.

The amounts of Family Support, GMFI and IFTC will be shown separately on the certificate of entitlement issued by the Commissioner.

If a family's income is within the abatement range, the amount of the abatement will first be assigned to the Family Support entitlement, and only when there is no Family Support entitlement left to abate will the IFTC amount begin to be abated.

Abated family support for beneficiaries

Beneficiaries who currently receive an income-tested benefit may choose to receive either full or zero Family Support from New Zealand Income Support Service (NZISS).

In order to treat beneficiaries the same as non-beneficiary Family Support recipients, beneficiaries will now be able to receive abated Family Support. If NZISS considers that a beneficiary's income exceeds \$20,000 a year, the payment of Family Support will be abated.

Until NZISS systems can be amended to pay abated Family Support, beneficiaries whose income exceeds \$20,000 will have their Family Support entitlement from NZISS cancelled and asked to apply to Inland Revenue for their Family Support entitlement. Inland Revenue will calculate their abated entitlement and pay it to them. Beneficiaries who receive Family Support from Inland Revenue will have to file an income tax return at the end of the income year.

Guaranteed minimum family income

Section KD 3 Income Tax Act 1994

Introduction

Guaranteed minimum family income (GMFI) will rise from \$278 (after tax) a week to \$284 a week from 1 July 1996, and to \$290 per week from 1 July 1997.

Background

GMFI tax credit supplements the incomes of low wage working families with dependent children. To qualify, a person must work a required number of hours (20 hours for a sole parent or 30 hours combined for a couple). The credit currently provides a guaranteed after-tax income of \$278 per week (\$14,456 per annum), with Family Support being paid on top of this tax credit.

The level of GMFI is to be increased to pass on the benefit of tax cuts to low wage families.

Key features

On 1 July 1996 the GMFI rate will be increased to \$284 per week. The composite rate for the 1996-97 income year will be \$14,690.

On 1 July 1997 the GMFI rate will be increased to \$290 per week. The composite rates for the 1997-98 income year will be \$15,002.

For the 1998-99 income year and subsequent income years the GMFI level will be \$15,080 a year.

Changes to the GMFI formula

The GMFI entitlement formula has been simplified by removing the references to Family Support.

The definition of net specified income has also been changed. The new formula grosses up the assessable income for the period, but instead of taking away actual tax paid from the grossed up income, the amended formula takes off the tax that would have been paid on the grossed up income. The only rebate which is taken into account in the calculation of the tax that would be payable is the low income rebate.

Part 3 - Surcharge and pension changes

New Zealand Superannuitant surcharge (Section JB 3 (1), JB 4 (1), NI 5 Income Tax Act 1994)

Introduction

The threshold above which the New Zealand Superannuitant surcharge applies has been increased from \$80 per week for a single superannuitant to \$90 from 1 July 1996, and \$100 from 1 July 1997. For a couple, the threshold has been increased from \$120 per week to \$135 from 1 July 1996 and to \$150 with effect from 1 July 1997.

Background

The amendments to the New Zealand Superannuitant surcharge give effect to the policy measures announced by the parties to the Accord on Retirement Income Policies on 4 December 1995.

The increases in the surcharge exemption on 1 July 1996 and 1 July 1997 are expected to result in about 20,000 fewer superannuitants being liable for the surcharge in 1998-99 than would be liable under the current thresholds. Those who do not have their superannuation completely abated by the surcharge will benefit from this measure, and there will be reductions in liability for those who continue to be liable.

Key features

1 July 1996

From 1 July 1996 the current single person exemption of \$80 a week will increase to \$90 a week, and the

couple exemption will increase from \$120 a week to \$135 a week.

The composite annual exemption for the 1996-97 income year will be \$4,550 for a single person (\$87.50 per week), and \$6,825 for a couple (\$131.25 per week).

1 July 1997

From 1 July 1997 the single person exemption will increase by a further \$10 to \$100 per week, and the couple threshold will increase a further \$15 to \$150 a week.

The composite annual exemption for the 1997-98 income year will be \$5,070 for a single person (\$97.50 per week) and \$7,605 for a couple (\$146.25 per week).

1 April 1998

The surcharge exemption for the 1998-99 income year and subsequent years will be \$5,200 for a single person (\$100 per week) and \$7,800 for a couple (\$150 per week).

Changes to surcharge codes

The surcharge codes which apply to source deduction income (other than New Zealand Superannuation) are amended to take into account the increase in the thresholds.

Qualifying foreign private annuities - income tax and surcharge treatment Sections CG 15, JB 2, JB 3 and OB 1, Income Tax Act 1994 Sections 245R and 245RA, Income Tax Act 1976

Introduction

New rules relating to the income tax and New Zealand Superannuitant surcharge treatment of foreign-sourced private pensions, and annuities have been introduced into the Income Tax Act 1994 and the Income Tax Act 1976.

Certain foreign private pensions and annuities derived from an interest in a qualifying foreign private annuity (QFPA) are now excluded from the foreign investment

fund (FIF) regime. Instead, they will be subject to tax on a receipts basis, in the same manner as income derived from salary or wages. In addition, only fifty percent of the gross pension or annuity will be subject to surcharge.

Background

The amendments follow recommendations made to the Government by the parties to the Accord on Retirement Income Policies (the Accord).

Previously, with some limited exceptions, all resident taxpayers who received a foreign pension or annuity had an interest in a FIF. This required disclosure of the interest to Inland Revenue, together with a calculation of the taxpayer's FIF income attributable to his or her interest in the FIF. The FIF income was also fully subject to surcharge.

The Accord parties were concerned that the previous treatment of foreign pensions was not consistent with paragraph 3.2.1 of the Accord. That paragraph states:

In regard to New Zealand taxation and the surcharge, a foreign-sourced private pension should have no advantage or disadvantage over a New Zealand-sourced private pension.

In addition to the concerns raised by the Accord parties, the Government was concerned that residents who received foreign pensions and annuities were not aware they had an interest in a FIF and were subject to that tax regime.

To address these concerns, the Government agreed to introduce amendments to exclude certain foreign-sourced private pensions and annuities from the FIF regime and to make only fifty percent of these pensions subject to surcharge. Not all foreign pensions qualify for this treatment. This is explained further in the appendix to this TIB, which relates to the definition of a QFPA.

Key features

An interest in a foreign superannuation scheme or life insurance policy that is an interest in a QFPA is excluded from the FIF regime.

Pensions and annuities derived from a QFPA will now be subject to income tax on a receipts basis. Only fifty percent of the gross amount of these pensions and annuities will be subject to the surcharge.

The amendments apply from the beginning of the FIF regime.

Persons who were complying with the FIF regime have until the due date for filing their 1997 return of income to elect to stay with the FIF regime for the income years from the beginning of the FIF regime until the end of their 1995-96 income year. They are also entitled to elect irrevocably to continue to return their pension or annuity under the FIF regime.

These features are given effect in the legislation as follows:

- A new definition of "qualifying foreign private annuity" (QFPA) is inserted into section OB 1.

- Section CG 15 (2) (which exempts certain interests in foreign entities from the FIF regime) is amended to exclude interests in a QFPA from the FIF regime.
- The section OB 1 definition of an "Interest in an employment-related foreign superannuation scheme" (ERFSS) is amended to ensure that if an interest meets both the definition of an ERFSS and a QFPA, the QFPA treatment takes precedence.
- The definition of "other income" in section JB 3 is amended to *exclude* one-half of any amount received from a QFPA.
- The definition of "net New Zealand Superannuation surcharge" in section JB 2 is amended to *include* one-half of any amount received from a QFPA.
- For surcharge purposes the concessional surcharge treatment is also extended to those interests in foreign entities which meet both of these conditions:
 - They do not meet the definition of an interest in a FIF because of the exclusions in section CG 15 (2)(d) to (f).
 - They are received by a person who is in breach of the non-resident contributions test in paragraph (a) of the QFPA definition.

Application date

The amendments made to sections CG 15 (2) and OB 1 apply retrospectively from the beginning of the FIF regime. This means they apply from the 1992-93 income year for most taxpayers, or from the 1991-92 income year for taxpayers whose corresponding non-standard accounting year ends after 2 July 1992.

Because of the retrospective application of the amendments to the FIF regime, it was necessary to amend both the 1976 and 1994 Income Tax Acts.

The amendments have retrospective application because some people who received a foreign pension or annuity did not realise that the FIF regime applied, and reported their income on a cash-receipts basis. However, people who have complied with the provisions of the FIF regime may elect to continue with that regime.

The amendments to the surcharge provisions, namely sections JB 2 (3) and JB 3 (1), apply from the beginning of the 1996-97 income year.

A more detailed analysis of these changes is contained in the appendix to this TIB.

Part 4 - IR 5 non-filing requirements simplified

Section IC, OB 1, OB 4 Income Tax Act 1994

Section 22(3), 33, 33A, 41 Tax Administration Act 1994

Introduction

The requirements an IR 5 taxpayer must meet to be exempt from filing a tax return have been simplified for the 1995-96 income year. The income threshold for compulsory filing by IR 5 taxpayers other than superannuitants will be increased from \$20,000 to \$34,200 for the 1996-97 income year, and to \$38,000 for the 1997-98 income year. Taxpayers who are subject to the superannuitant surcharge, Family Support recipients, liable parents and Student Loan borrowers are still required to file tax returns.

Background

Both the Government and Inland Revenue have a commitment to simplifying the tax system and minimising compliance costs. A key area in the simplification of the tax system is the simplification of tax return filing obligations for individuals, which has two objectives:

- to reduce the number of taxpayers required to file tax returns
- to simplify tax returns for taxpayers who are still required to file.

The amendments described here represent the first step in this process. The Government has issued a discussion paper on the further expansion of non-filing to IR 5 taxpayers whose income is over \$38,000, and to IR 5 taxpayers to whom social policy measures such as Family Support and the Student Loan scheme apply.

Key features

1995-96 income year

A new section 33A has been inserted into the Tax Administration Act with effect from the 1995-96 income year. The section sets out the criteria a natural person must meet to be exempted from the requirement to file a tax return. This provision is effectively the old pay-period taxpayer definition clarified, with a number of minor simplifications. The pay-period taxpayer definition has been repealed.

New non-filing rules

The new section 33A(1) provides the rules that taxpayers must meet to be exempted from the requirement to file a tax return. The main requirements are that a person must derive income from these sources only:

- employment from which tax deductions were liable to be made in accordance with the PAYE rules
- interest or dividends from which resident withholding tax was liable to be deducted in accordance with the PAYE rules.

Further, the person's total income must not exceed whichever of the following applies:

- \$9,500 (regardless of the source of the income)
- \$20,000 (if all the income was from employment)
- \$20,000 (if there was not more than \$1,500 of interest included in the income).

Further, the person will have to file a return if he or she meets any of these conditions:

- derives income as a shearer or as a shearing shed hand
- is an absentee
- has a family certificate of entitlement or a spouse who has a family certificate of entitlement
- is liable to pay Child Support
- has a Student Loan balance with Inland Revenue
- is a superannuitant with more than \$3,120 of other income.

The other income of a superannuitant is defined as income from:

- employment (other than NZ superannuation)
- interest and dividends
- 50% of any pension from a superannuation fund and 50% of any annuity which section CB 9 (f) applies (annuities paid under a life insurance policy entered in to or offered in New Zealand by a life insurer, or offered or entered into outside New Zealand by a life insurer that is resident in New Zealand).

Previously the pay-period taxpayer definition required that a tax deduction be made in respect of all income from employment in accordance with the PAYE rules. In effect, this provision placed an obligation on the employee to ensure that the employer was correctly deducting PAYE. The new provision simply requires that employment income be liable to deduction in accordance with the PAYE rules. A similar amendment has been made in relation to interest.

The new section provides for two situations in which a person must file a return.

- A tax return must be filed if a person or the spouse of that person receives abated Family Support from NZISS. This provision is required because the joint impact of the changes in the benefit abatement rules and the increase in this maximum income threshold above which a tax return must be filed means that it is possible for a beneficiary to earn over \$20,000 income and thus be entitled only to abated Family Support. Without a tax return from this beneficiary it would be

impossible to ensure that a family receives its correct Family Support entitlement.

- Taxpayers who have received a special tax code must file a tax return. While this has been the Commissioner's policy, the previous legislation allowed the Commissioner to request a return from taxpayers with special tax codes only if he was satisfied that the tax code was invalid when applied in determining a tax deduction.

Consequential amendments

References to the term "pay-period taxpayer" have been removed and, where necessary, references to the new section 33A have been inserted. The amendments apply from 1 April 1995.

1996-97 income year

For the 1996-97 income year the non-filing income threshold is raised from \$20,000 to \$34,200, which is the boundary between the bottom and top statutory marginal tax rates for that year. The distinction between income from interest and dividends and income from employment is also removed.

This non-filing income threshold applying to superannuitants is increased from \$3,120 to \$3,412.50 for the 1996-97 income year. The increased threshold represents the minimum possible surcharge exemption applying to a married superannuitant for that year, ensuring that those with a potential NZ Superannuitant surcharge liability are required to file.

1997-98 income year

The non-filing income threshold for the 1997-98 and subsequent income years is further increased to \$38,000.

Again, the extra non-filing income threshold applying to superannuitants is increased from \$3,412.50 to \$3,802.50.

1998-99 income year

For the 1998-99 income year the non-filing income threshold applying to superannuitants' other income increases to \$3,900. This final increase is required as the surcharge threshold applying in the 1997-98 income year was a composite threshold, so the extra filing threshold was effectively a composite rate as well.

Part 5 - Minor correction to rebate abatement calculation

Section KB 3 Income Tax Act 1994

A minor amendment confirms that if the calculation of a rebate results in a negative amount, the rebate amount will be treated as zero and not a negative number for the purposes of determining that rebate. This corrects a

minor drafting error which meant that it was technically possible for a taxpayer's abatement to exceed the amount of rebate for which he or she qualified.

This amendment applies from 1 July 1996.

Part 6 - Family Support and unsupported children

Section OB 1, Income Tax Act 1994/Section 374A, Income Tax Act 1976

Introduction

The amendment prevents the continued payment of Family Support and guaranteed minimum family income for children for whom orphan's benefit or unsupported child's benefit is being paid. It corrects an unintended legislative change that allowed Family Support to be paid for children for whom orphan's benefit or unsupported child's benefit is also being paid, which has resulted in double state funding of some families.

Background

Legislation pertaining to the entitlement and payment of Family Support and guaranteed minimum family income (GMFI) is contained in Part KD of the Income Tax Act 1994 and Part XIA of the Income Tax Act 1976.

Changes to the Family Support legislation in 1991, when family benefit was abolished, inadvertently allowed Family Support and GMFI to be paid for a child for whom orphan's benefit or unsupported child's benefit is paid.

Before the abolition of family benefit, Family Support and GMFI were payable only for a child for whom family benefit was payable. Because family benefit was not payable for a child for whom orphan's benefit or unsupported child's benefit was being paid, Family Support and GMFI were not payable for such a child.

Key features

The amendment prevents principal caregivers claiming Family Support and GMFI for children for whom orphan's benefit or unsupported child's benefit is being paid. This is achieved by excluding such children from the definition of "dependent child" in section OB 1 of the

Income Tax Act 1994 and section 374A of the Income Tax Act 1976. Because Family Support and GMFI are payable only for a "dependent child", they will not be payable for these children.

Application date

The amendment generally applies from the income year beginning 1 April 1991 to prevent principal caregivers who have not already received Family Support for such children from doing so. The exceptions to the general application date are as follows.

- Principal caregivers who, before the date of introduction of the bill (12 December 1995), had applied for an income-tested benefit and Family Support for the 1995-96 income year to NZISS for a child for whom orphan's benefit or unsupported child's benefit is being paid were entitled to family support until 31 March 1996.
- Principal caregivers who have a current year certificate of entitlement for Family Support and GMFI in respect of a child for whom orphan's benefit or unsupported child's benefit is being paid were entitled to Family Support until 31 March 1996 if that certificate was held or applied for before the date of introduction of the bill.

Family Support received for such children after 31 March 1996 will therefore need to be repaid.

Principal caregivers who have claimed Family Support and GMFI in the 1994-95 income year before 12 December 1995 as part of the Family Support end-of-year square-up for a child for whom orphan's benefit or unsupported child's benefit is being paid, may also claim Family Support and GMFI for that child as part of the 1995-96 income tax returns and Family Support statement.

*T*AX INFORMATION BULLETIN

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This TIB outlines the changes which have resulted from the enactment of the Tax Reduction and Social Policy Bill and the Finance Bill (No.6).

The Tax Reduction and Social Policy Bill was enacted on 10 May 1996. It was split into the following Acts:

- Income Tax Act 1994 Amendment Act 1996
- Income Tax Act 1976 Amendment Act 1996
- Tax Administration Amendment Act 1996
- Social Security Amendment Act
- Social Welfare (Transitional Provisions) Act 1996.

This TIB deals only with the tax changes which have occurred; it does not cover the changes to the Social Welfare legislation.

The Finance Bill (No.6) was enacted on 1 July 1996. The bill became the Income Tax Act 1994 Amendment Act (No.2) and the Income Tax Act 1976 Amendment Act (No.2)

This TIB is broken down into six parts and an appendix. The first five parts deal with the changes which have resulted from the Tax Reduction and Social Policy Bill. The sixth part deals with the changes resulting from the Finance Bill (No.6).

The appendix provides an in-depth analysis of the amendments to the tax treatment of foreign-sourced private pensions.

See the inside cover for a full list of this TIB's contents.

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